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September 15, 2008

AGENDA ITEM 11a

TO: MEMBERS OF THE INVESTMENT COMMITTEE

I. SUBJECT: Enhancements to Investment Line-Up

II. PROGRAM: Supplemental Income Plans (SIP)

III. RECOMMENDATION: Information Only

Wilshire Associates' opinion letter is shown in Attachment 1.

IV. ANALYSIS:

Background

The Supplemental Income Plans (SIP) Division administers the CalPERS 457 Plan, the Supplemental Contributions Program (SCP) and the Peace Officers and Firefighters (POFF) Plan. Last year the 457 and the SCP Plans' fund offerings were changed in phase I of the fund enhancements, with additional enhancements planned for 2008. The POFF plan enhancements that will take effect on October 6, 2008, were reported to the Investment Committee on August 18, 2008. All the changes focused on optimizing CalPERS in-house investment expertise while keeping fees low and offering improved performance for the benefit of participants. This agenda presents the phase II fund line-up for the 457 Plan and the SCP.

The 457 Plan is offered to public agencies and schools throughout the State of California. Its service model includes a dedicated phone line as well as a custom transactional website. In addition, CalPERS provides Plan Account Managers to meet with employees at their work sites for educational presentations and one-

on-one enrollment meetings. During the 2006/2007 fiscal year, Account Managers met with 4731 participants and presented 229 educational sessions. As of July 31, 2008, there were 26,700 participants and 660 local agencies and schools participating in the CalPERS 457 Plan.

The SCP is offered to the State of California CalPERS members, Judges Retirement System (JRS) members, JRS II members, and Legislators' Retirement System members. The SCP service includes a dedicated phone line and a custom transactional website introduced in 2007. As of July 31, 2008, there were 729 participants in the Plan.

New fund line-up

Below is the investment line-up and fees to be offered to the 457 Plan participants on November 3, 2008.

457 Plan Fund Line-up			
Current Fund	Current Fee	New Fund	New Fee
Fixed Income Funds			
CalPERS Total Return Bond	0.55%	CalPERS Total Return Bond	0.55%
CalPERS TIPS	0.55%	CalPERS TIPS	0.55%
SSgA Stable Fixed Income	0.51%*	PIMCO Moderate Duration Stable Value**	0.51%
Equity Funds			
CalPERS S&P 500 Index	0.35%	CalPERS S&P 500 Index	0.35%
Turner Active Large Cap Growth	0.90%	Turner Active Large Cap Growth	0.90%
AllianceBernstein Active Large Cap Value	0.90%	AllianceBernstein Active Large Cap Value	0.90%
CalPERS Small & Mid Cap Index	0.40%	CalPERS Small & Mid Cap Index	0.40%
		The Boston Co Small & Mid Cap Growth	0.98%
		The Boston Co Small & Mid Cap Value	0.98%
CalPERS International Index	0.40%	CalPERS International Index	0.40%
SSgA Select Active International	0.94%*	Pyramis International Select	0.94%
Asset Allocation Funds			
SSgA Risked-Based: Conservative, Moderate, Aggressive	0.64%*	CalPERS Risked-Based: Conservative/Moderate/Aggressive	0.64%
SSgA Target Retirement Date: Income, 2010, 2020, 2030, 2040	0.64%*	CalPERS Target Retirement Date: Income, 2005, 2010, 2015, 2020, 2025, 2030, 2035, 2040, 2045, 2050	0.64%

* In addition, the Fund is charged an annual custody fee and such other fees and expenses as permitted by the Declaration of Trust.

** Due to contractual limitations, existing Stable Value assets will be transitioned from the existing SSgA fund to the PIMCO fund over a 12-month period.

The CalPERS managed funds will increase from five to nineteen funds in this fund line-up. The increase in CalPERS managed funds is a result of the availability of the new CalPERS asset allocation funds approved by the Investment Committee at the August 18, 2008 meeting. These funds include the CalPERS Risk-based funds and the CalPERS Target Retirement Date funds. They allocate assets based on a participant's risk tolerance or retirement date to underlying funds that are either CalPERS managed funds or externally managed funds offered in the Plan line-up.

These funds are superior products in comparison to the funds they will replace for no additional cost to participants. Among the notable characteristics of the new funds are the following:

- The wide range of asset classes to be included is found in few existing asset allocation funds. The additional asset classes utilized by the funds are expected to lower volatility through broader diversification and provide additional inflation protection. These asset classes will include equity, fixed income, Stable Value, TIPS, Emerging Markets, REITS and Commodities.
- The funds will include a blend of externally-managed active and CalPERS-managed active and passive underlying funds. Actively-managed funds will provide opportunities to enhance returns while passively managed funds help keep costs low.

In addition, four new active external managers will be added to the line-up. This includes two small-mid cap equity managers, one international equity manager and a stable value manager. These external managers will offer a greater selection of active strategies for participants and have displayed strong historical performance track records.

The SCP Plan will get the same fund line-up as the 457 Plan on March 2, 2009. The current SCP Fund offered since the Plan's inception will be transferred to the CalPERS Moderate Risk-based fund. This new fund will offer a similar asset allocation with additional asset classes to offer better risk adjusted returns and broader diversification for improved diversification and reduced risk.

Fees

Fees charged to participants will be reduced with the implementation of the new fund line-up. The new funds will no longer include externally managed funds with commingled structures which include embedded fees for custodial and other services. These fees were set and controlled by the external manager and

varied by the number of participants in the funds. The average fee was 0.07% per year and was deducted directly from the participants' accounts. The new CalPERS funds will be accounted for in a separate account structure under the direction of CalPERS.

As the number of funds and the complexity will increase with the asset allocation funds, custody costs will increase by \$391,000. This is less than 13 percent of the current contract amount and within delegated authority for staff approval. This cost can be absorbed within the fee structure of the new fund line-up. This is possible due to the lower expense of using CalPERS Investment Office staff for investment management rather than paying an external manager for these services.

V. STRATEGIC PLAN:

This agenda's initiatives address multiple CalPERS Strategic Plan Goals including:

- Goal (VI) to Administer pension benefit services in a customer oriented and cost effective manner;
- Goal (VII) to Enable and educate members and employers to make informed decisions leading to a predictable and secure retirement futures; and
- Goal (IX) to Achieve long-term, sustainable, risk adjusted returns.

VI. RESULTS/COSTS:

The revised investment line-up will provide expanded and improved investment options at lower cost to participants.

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